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In The
SUPREME COURT OF THE UNITED STATES

October Term, 1973

No. 73-485

IN THE MATTER OF
LESLIE STEVEN KOVATS, Bankrupt,
Petitioner,

vs.

FIRST NATIONAL BANK OF BROKEN ARROW,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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In The
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No.

IN THE MATTER OF
LESLIE STEVEN KOVATS, Bankrupt,
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vs.

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Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

TO THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your Petitioner, Leslie Steven Kovats, hereinafter referred to as "Petitioner", hereby petitions for a Writ of Certiorari to review the Decision of the United States Court of Appeals for the Tenth Circuit. That Court of Appeals, on direct appeal, reversed and remanded with directions to reinstate the Certificate Order of the Ref-

eree entered on March 7, 1972, thereby reversing the Order of the United States District Court for the Northern District of Oklahoma which Order adopted the Report and Recommendations of the United States Magistrate making Findings of Fact and Conclusions of Law granting a discharge in bankruptcy to Petitioner of the claim of the First National Bank of Broken Arrow.

OPINIONS BELOW

The opinion of the Court of Appeals was filed June 19, 1973, and although it was a per curiam opinion, it is ordered not to be reported. A copy of said opinion is appended hereto as Appendix A.

The Order of the Referee in Bankruptcy incorporating by reference Findings of Fact and Conclusions of Law, ordering that the debt owed by Petitioner to the First National Bank of Broken Arrow is not dischargeable in Bankruptcy and awarding judgment to the aforesaid bank was filed March 7, 1972, a copy thereof together with a copy of the Findings of Fact and Conclusions of Law which was filed on March 3, 1972, are appended hereto as Appendix B.

The Order of the United States District Court for the Northern District of Oklahoma adopting the Report and Recommendations of the United States Magistrate making Findings of Fact and Conclusions of Law and granting a discharge in bankruptcy to Petitioner of the claim of the aforesaid bank is unreported and was filed June 21, 1972, a copy thereof is appended hereto together with the Report and Recommendations of the United States Magistrate which was filed June 19, 1972, as Appendix C.

JURISDICTION

The judgment of the Court of Appeals which Petitioner seeks to have reviewed was made and entered on June 19, 1973. An order denying a timely petition for rehearing was made and entered by said Court of Appeals on August 1, 1973. The statutory provision believed to confer jurisdiction on this Court to review the judgment in question is 28 U.S.C. Sec. 1254(1).

QUESTIONS PRESENTED FOR REVIEW

1. In connection with a determination under Sec. 17(a)(2) of the Bankruptcy Act, 11 U.S.C. Sec. 35(a)(2), was a finding by the Referee in Bankruptcy, resolving a conflict in the evidence as to whether the bankrupt's false written statement respecting his financial condition was delivered to the lending bank before or soon after the consummation of the original loan, necessary to an ultimate finding that the false statement when delivered to the bank was made with the intent to deceive?

2. Did the bankrupt's oral statement to the lending bank (which was made approximately seven months after the original loan and on the occasion of the renewal of said loan) that there had been no change in his financial condition entitle the bank to rely on the false written statement absent findings that the false written statement had been delivered to the bank prior to the consummation of the original loan and that at the time of the delivery thereof it was made with the intent to deceive?

3. Where the Referee in Bankruptcy failed to make the basic Findings of Fact necessary to support his ultimate Findings and Conclusions, was the District Court on review entitled to supply and make the missing basic findings and on the basis thereof reverse the Referee's decision?

4. Is the Court of Appeals' decision in conflict with decisions of the Oklahoma Supreme Court and of other Federal Courts in regard to the elements of proof necessary to establish fraudulent intent to deceive as a bar to discharge in bankruptcy?

STATUTES INVOLVED

Involved are Title 11, United States Code, Sec. 35(a)(2) and Title 11, United States Code, Sec. 32(c). These provisions are reproduced in Appendix D hereto.

STATEMENT OF THE CASE

The undisputed facts are:

(1) On October 15, 1970, Respondent bank loaned Petitioner $20,000.00 evidenced by Petitioner's Promissory Note of that date for said amount payable in six months which was guaranteed by Petitioner's employer, Braden Industries;

(2) Either shortly before or shortly after the consummation of said loan Petitioner submitted to Respondent a false financial statement;

(3) On May 19, 1971, Petitioner renewed said loan by executing and delivering to Respondent a renewal note for said amount also guaranteed by his employer;

(4) At the time of said renewal, Petitioner, in response to Respondent's inquiry, orally stated that there had been no change in his financial condition since making the original loan and at that time Respondent requested a new financial statement which Petitioner submitted more than a month later;

(5) On or about September 2, 1971, Petitioner filed his Petition in Bankruptcy in the United States District Court

for the Northern District of Oklahoma, listing therein Respondent as an unsecured creditor in the amount of $20,000.00;

(6) After hearing on Respondent's objection to Petitioner's discharge, the Referee in Bankruptcy held that said indebtedness was not dischargeable and rendered judgment in favor of Respondent for the amount of $20,838.38 as the balance due on said indebtedness.

The evidence was conflicting as to whether the false financial statement was submitted to Respondent before or after the original loan had been consummated. The Referee, being unable (on the basis of the evidence before him) to resolve this conflict in the evidence, made no finding of fact on the question of when the statement was delivered and whether Respondent relied on it in making the original loan. The Referee held that such findings were unnecessary since the Respondent, when it renewed the loan seven months later, relied on the false statement as originally submitted and on Petitioner's oral statement that there had been no subsequent change in his financial condition and further held that such was sufficient to establish Petitioner's fraudulent intent when the written statement was originally submitted and that the debt was not dischargeable.

On review of the Referee's findings and decision, the District Court in reversing the Referee's findings and decision upheld Petitioner's contention that the Referee's failure to make these findings were fatal to his ultimate decision that the indebtedness was not dischargeable because, without a finding that the statement had been submitted prior to the consummation of the original loan, there would be no basis for a finding that the statement was made with intent to deceive or that the Respondent relied on it in making said loan or that Respondent was

justified to rely on it seven months later when Respondent renewed the loan. In other words - if the Referee had found (as Petitioner testified) that the financial statement was not requested by Respondent until after the loan had been consummated and was submitted on the basis of Respondent's statement that it was merely a formality to satisfy the bank's auditors and that the bank was satisfied to rely on the guarantee of the loan by Petitioner's employer - there was lacking any intent (as required by Clause 2 §17a. of the Bankruptcy Act) by Petitioner to deceive and hence the statement was not made or relied on as an inducement to Respondent in making the loan or the renewal thereof.

The United States Court of Appeals reversed the District Court's decision and reinstated the Referee's findings and decision. The reasoning of the Court of Appeals will be considered in detail in the Argument set forth below.

ARGUMENT

In view of the conflict in the evidence as to when Petitioner's written financial statement was delivered to Respondent (Petitioner testified that such a statement was not requested until after the loan had been made and that the statement was requested only as a formality to satisfy auditors, while an officer of Respondent testified that he had received the statement prior to making the loan) - a finding as to whether Petitioner's financial statement was delivered prior to or after the consummation of the October 15, 1970, loan is essential to a decision finding that the false financial statement delivered to the Respondent was made with the intent to deceive. In the absence of such a finding, the Referee's Decision and Order which was reinstated by the Court of

Appeals cannot stand. If the statement was delivered after the loan was consummated, it would follow that it was not given with the intent to defraud or to obtain the credit which Petitioner had already received. Without such intent the Respondent's reliance on the statement 7 months later in granting the renewal of the original loan, cannot be the basis for denial of discharge.

If the necessary intent was lacking at the time of delivery, the Respondent's case fails for it must establish by preponderance of the evidence that it relied upon a false statement in writing made with the intent to deceive. See *Sweet* v. *Ritter Finance Company* 263 F.Supp. 540 (W.D. Va. 1967), at p. 543 wherein the Court held as follows:

> "...it is apparent from the evidence presented that Ritter Finance has failed to prove two additional elements necessary to make a debt nondischargeable under §17(a)(2), namely, that there was a reasonable reliance on the financial statement by Ritter Finance and that there actually was fraudulent intent to deceive on Sweet's part. The absence of either element is enough to support a judgment for Elack Sweet in this case."

Without a finding by the Referee that the financial statement was delivered to the Respondent prior to the consummation of the original loan, there is no basis for an ultimae finding that the statement was "made or published or caused to be made or published with the intent to deceive". In view of the Referee's failure to make findings on the questions, the District Court on review made appropriate findings. In view of the Referee's failure to make the basic findings required to support his ultimate conclusion, the Referee's Decision and the Court of Appeals' reinstatement of said Decision are clearly erroneous and should be reversed.

In making the renewal loan, the bank was not justified in relying on a financial statement given seven months prior thereto by Petitioner. 37 Am. Jur. 2d, Fraud and Deceit §243, states:

> "...In general, where the relationship of the parties comprises a single transaction, and a financial statement is submitted for that purpose, representations therein made are not to be considered continuing or applicable to a time other than that of the transaction or submission".

Monier v. *Guaranty Trust Co. of New York*, 82 F.2d 252 (2nd Cir. 1936) at p. 254 follows this rule holding:

> "...This contention is that when the plaintiffs gave their March 31 statement to Sample it carried an implied representation that 'this fairly reflects our present condition on June 13.' Such an implication from the mere handing over of a financial statement is not, in our opinion, justified. The statement on its face shows that it represents conditions on a certain date..."

If the financial statement here in question had contained a provision that it may be deemed to continue to reflect the Petitioner's financial condition unless notification is given to the contrary (as most bank financial statement forms do) the Respondent might have been entitled to rely on the financial statement in subsequent transactions. But in the absence of any such provision, the reasonable understanding is that the financial statement speaks as of its date and is limited to the transaction for which it was given. Consequently, the Respondent was not justified in relying on such a statement in connection with a subsequent transaction.

The evidence in the case at bar shows that the Respondent at the time of the making of the renewal note

requested a new and updated financial statement but that the new financial statement was not received until more than a month after the renewal had been made. By this the Respondent indicated to Petitioner that it was not relying on the first statement, instead that it relied on Petitioner's *oral* statement, made at the time of the making of the renewal loan, that there was no change in his financial condition.

In *International Shoe Co.* v. *Kahn*, 22 F.2d 131 (4th Cir. 1952) at p. 133 the Court held that considering the exigencies of business affairs, and the general practice current in busines circles, it would be unreasonable to construe a financial statement as continuing indefinitely, in the absence of a clear expression of intent in the instrument itself and that republication of the statement, if any there was, would have to be inferred soley from the bankrupt's purchase in 1925, and his breach of the promise to communicate a change in financial condition. The Court further held that reprehensible as this course of dealing may have been, assuming that the promise to communicate change of financial condition was still effective, *it did not amount to the issuance of a false statement in writing*. The Court further held that it must be borne in mind that it is not enough to prove breach of contract, or even deliberate fraud. That oral statements or conduct of the bankrupt, no matter how false or fraudulent, are not within the terms of the statute. A false writing must be proved if the discharge of the bankrupt is to be refused, under Section 14(c) of the Bankruptcy Act which is similar to Sec. 17(a)(2) of the Bankruptcy Act with respect to financial statements.

In the case at bar, Petitioner's alleged oral statement on May 19, 1971, that there had been no change in his fianancial condition since his earlier written

statement was not a remaking, renewal or reissuance *in writing* of the earlier statement. Consequently, the Referee's finding that the bank in granting the renewal loan on May 19, 1971, relied on a false financial statement in writing was contrary to the evidence. The Referee made no finding that the written statement when given was intended to mislead or was intended to be relied upon in future credit transactions. Absent these findings, the Referee's ultimate Findings and Conclusions were clearly erroneous and the Court of Appeals erred in reversing the District Court and reinstating the Referee's Order.

Where the Referee failed to make the basic findings of fact necessary to support his ultimate Findings and Conclusions, the District Court on review had ample authority to supply the missing basic findings and on the basis thereof could properly find that the Referee's ultimate Findings and Conclusions were clearly erroneous and reverse the Referee's Decision and Judgment. In *Gerdes* v. *Lustgarten*, 266 U.S. 321, at p. 327, this Honorable Court said:

> "The question now arises as to what disposition we should now make of the case. The material questions of fact in reference to the financial statement, upon which the decision must ultimately depend, have not as yet been determined in the courts below. They were not decided by the referee who heard the testimony; they were apparently assumed by the District Court; and they were not passed upon by the Circuit Court of Appeals on account of this ruling in reference to the lapse of time. We may now either determine these questions upon an independent examination of the testimony, or remand the case for further proceedings in order that they may be determined in the lower courts..."

The Oklahoma Supreme Court in the case of *Wheeler & Motter Merchantile Co.* v. *Green*, 222 P. 965 (Okla. 1924), in passing on the question as to the elements of proof necessary to establish the existence of fraud sufficient to bar a discharge in bankruptcy said at p. 966:

> "...This court has held that to constitute actionable fraud, the following must be made to appear:
>
> '(1) That defendant made a material representation; (2) that it was false; (3) that when he made it he knew that it was false, or made it recklessly, without any knowledge of its truth and as a positive assertion; (4) that he made it with the intention that it should be acted upon by plaintiff; (5) that plaintiff acted in reliance upon it; (6) that he thereby suffered injury; and (7) all these facts must be proven with a reasonable degree of certainty, and all of them must be found to exist; the absence of any of them would be fatal to a recovery.' Wingate v. Render, 58 Okl. 656, 160 Pac. 614; Henry v. Collier (Okl. Sup.) 169 Pac. 636; Cooper v. Gibson (Okl. Sup.) 170 Pac. 220."

In the case at bar there is lacking evidence sufficient to establish, and there is no finding as to, the fourth element (above referred to) that the Petitioner made a false statement "with the intention that it should be acted upon by plaintiff" and there is no evidence or finding as to the sixth element that Respondent has "thereby suffered injury".

On the question of Petitioner's intention, he testified that the statement was given pursuant to Respondent's request made subsequent to the loan and that (according to Respondent) the purpose was merely a formality to

satisy the bank's auditors. Furthermore, the bank's evidence is that the grantor of the loan has assured it that regardless of the outcome of this case, the guarantor will honor its guarantee.

The United States District Court for the Western District of Virginia in *Sweet* v. *Ritter Finance Company, supra*, held at p. 543:

> "...Ritter Finance [the creditor] must prove actual fraud before it can show Swect's [the debtor] debt to be nondischargeable under §17(a)(2). In other words, Ritter Finance must show by a preponderance of the evidence that (1) the debtor made the representations; (2) that at the time he knew they were false; (3) that he made them with the intention and purpose of deceiving the creditor; (4) that the creditor relied on such representations and (5) that the creditor sustained the alleged loss and damage as the proximate result of the representations having been made. Friendly Finance Co. v. Stower, 109 Ga. App.21, 134 S.E. 2d 837 (1964). See also United States v. Syros, supra, and 1 Collier on Bankruptcy §17.16."

As pointed out in the *Wheeler & Motter Mercantile Co.* case, *supra*, the same elements of proof in the *Sweet*, *supra*, case and findings with respect thereto are missing in the case at bar. The conflict between the Court of Appeals' decision in the case at bar and the decisions of the Oklahoma Supreme Court and the United States District Court for the Western District of Virginia should be resolved by this Court.

CONCLUSION

It is respectfully submitted by the Petitioner that based upon the foregoing, the action taken by the Court

of Appeals was clearly in error and this Court should grant certiorari, and the Judgment of the Court of Appeals should be reversed with directions to reinstate the Judgment of the District Court.

Respectfully submitted,

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APPENDIX A

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

May Term, 1973

In the Matter of LESLIE STEVEN KOVATS, *Bankrupt*,
Appellee,

v.

FIRST NATIONAL BANK OF BROKEN ARROW,
Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF OKLAHOMA
(71-B-871)

Roger R. Scott, Tulsa, Oklahoma, (Pray, Scott & Livingston, Of Counsel, on the brief) for Appellant.

Irvine E. Ungerman, Tulsa, Oklahoma, (Ungerman, Grabel, Ungerman & Leiter and Fred W. Woodson, Tulsa, Oklahoma, on the brief) for Appellee.

Before LEWIS, Chief Judge; DURFEE*, Judge, Court of Claims; and HOLLOWAY, Circuit Judge.

PER CURIAM

*Sitting by designation.

This is an appeal from an order of the District Court for the Northern District of Oklahoma adopting a Report and Recommendation of the United States Magistrate reversing a Certificate Order by the Referee in Bankruptcy. The Referee had denied the dischargeability of a debt owed by appellee Kovats to appellant First National Bank of Broken Arrow.

Kovats filed a Debtor's Petition in Bankruptcy with the district court which was routinely referred to the Referee in Bankruptcy for consideration. The Bank then filed an Application to Seek Determination of Dischargeability of Debt pursuant to section 17(a)(2) of the Bankruptcy Act (11 U.S.C. §35). This section provides:

> (a) A discharge in Bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as ... (2) are liabilities for obtaining money or property by false pretenses or false representations or for obtaining money or property on credit or obtaining an extension or renewal of credit in reliance upon a materially false statement in writing respecting his financial condition made or published or caused to be made or published in any manner whatsoever with intent to deceive ...

The application sought a determination that the debt owed by Kovats to the Bank represented a liability for obtaining money by a materially false statement published with an intent to deceive the Bank.

On October 15, 1970, Kovats obtained from the Bank an unsecured $20,000 loan for six months. The Bank requested and received a written financial statement from Kovats. It is uncontested that the financial statement understated Kovats' liabilities by approximately $59,000. There is conflicting testimony as to whether the false

statement was given to the Bank before or after the original note was signed. The Bank also received a guaranty for Kovats' loan from his employer, Braden Industries.

The original loan was renewed for thirty days in April 1971 and for an additional six months in May 1971. When the note was renewed the Bank inquired of Kovats whether there had been any change in his financial condition. Kovats gave oral assurances to the Bank that his condition was still the same as that set forth in the original financial statement. A short time subsequent to Kovats' renewing his loan he furnished the Bank with another memorandum setting forth his financial condition.

After a hearing the Referee found that Kovats' original financial statement was inaccurate and misleading. The Referee did not resolve the conflict in testimony as to whether Kovats had given the Bank a copy of his financial statement prior to the granting of the original loan in October 1970. But, the Referee did find that the Bank relied on the false statement when renewing the loan in May 1971. The Referee held that section 17(a) of the Bankruptcy Act was clearly applicable and, therefore, the debt to the Bank was not dischargeable.

On appeal to the district court the matter was referred to the United States Magistrate for a hearing. The Magistrate heard oral argument but took no additional testimony. The Magistrate concluded that the Referee's findings were "clearly erroneous" and, accordingly, adopted new findings of fact and conclusions of law. The Magistrate's recommendation for reversal was accepted by the district court.

When the district court rejects the findings of a Referee as clearly erroneous, it is the duty of this court to apply the clearly erroneous standard to the findings of

the Referee rather than those of the district court. Potucek v. Cordeleria Lourdes, 10 Cir., 310 F2 527, 530; Clancy v. First National Bank of Colorado Springs, 10 Cir., 408 F2 899, 903, *cert. den.* 396 U.S. 958. After reviewing the record on appeal, we find that there is substantial evidence to support the Referee's findings of an intent by Kovats to deceive, and reliance by the Bank on the false financial statement when renewing the loan in question.

A district court when reviewing the order of a Referee is in an appellate posture. General Order in Bankruptcy 47 requires:

> Unless otherwise directed in the order of reference the report of a referee or of a special master shall set forth his findings of fact and conclusions of law, and the judge shall accept his findings of fact unless clearly erroneous.

Clearly, the district court's function is not to decide factual issues *de novo*. *Cf.* Zenith Radio Corp. v. Hazeltine Research, Inc., 395 U.S. 100, 123. Rather, the district court must review the findings and conclusions giving deference to the trier of fact who is in a superior position to weigh the evidence. This is especially true where, as in the instant case, the district court or magistrate did not take further testimony but only heard arguments of counsel. *Cf.* Washington v. Houston Lumber Co., 10 Cir., 310 F2 881, 882-883; Dailey v. City of Lawton, Oklahoma, 10 Cir., 425 F2 1037, 1039.

But, Kovats argues that it was necessary for the district court to make an additional finding as to when the original statement was delivered to the Bank. Without this finding, Kovats argues, it would be impossible for the Referee to determine whether the

Bank had relied on this statement in extending and renewing the loan. If the false financial statement was given after the consummation of the original loan then there was no intent to deceive by Kovats, nor could the Bank rely on the statement when granting the loan and renewing it seven months later. This argument flies in the face of facts and relative law.

We agree with the Referee that it was not necessary to resolve the conflict as to when the financial statement was delivered to the Bank. Section 17(a) of the Bankruptcy Act creates a bar to dischargeability if there is "an extension *or renewal of credit* in reliance upon a materially false statement in writing respecting his financial condition." (Emphasis added.) The record reveals that Kovats gave oral assurance when renewing the note that his financial condition had not changed during the previous seven months. The only statement in possession of the Bank was the one issued in October 1970, and testimony clearly reveals that it was regarding the financial picture as outlined in that false written statment to which the Bank's inquiry was directed. This evidence is sufficient to sustain the Referee's findings, and his holding is consistent with the requirements of section 17(a) of the Bankruptcy Act. Furthermore, section 17(a) does not require absolute or exclusive reliance on the false statement by the lending party as claimed by Kovats.It need be only a substantial factor in bringing about the extension of credit. Lloyd v. Industrial Bank, 2 Cir., 241 F2 924, 925; Wylie v. Ward, 9 Cir., 292 F2 590, 592; In re Clancy, D.C. Colo., 279 F. Supp. 820, 822; *aff'd sub nom.* Clancy v. First National Bank of Colorado,. 10 Cir., 408 F2 899, *cert. den.* 396 U.S. 958.

The judgment of the district court is reversed and the case remanded to the district court with directions to reinstate the Certificate Order of the Referee entered March 7, 1972.

APPENDIX B

**IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF OKLAHOMA**

IN THE MATTER OF:
LESLIE STEVEN KOVATS,
Bankrupt.

In Bankruptcy,
No. 71-B-871

ORDER

THIS MATTER comes on for hearing this 28th day of February, 1972, pursuant to Application To Seek Determination of Dischargeability of Debt filed herein by the First National Bank of Broken Arrow, a scheduled creditor in the captioned cause. Said creditor appeared by and through its President, Scott Graham, and its attorney, Roger R. Scott and Leslie Steven Kovats, the bankrupt, appeared in person and by his attorney, Fred W. Woodson. THEREUPON the court heard the evidence adduced at said hearing and the arguments of counsel and thereupon entered certain FINDINGS OF FACTS and CONCLUSIONS OF LAW which have been filed herein and which are incorporated as a part of this Order by reference.

Based upon the FINDINGS OF FACT and CONCLUSIONS OF LAW, it is hereby ORDERED, ADJUDGED and DECREED that the debt owed by Leslie Steven Kovats to the First National Bank of Broken Arrow, which is the subject of this proceeding, is not dischargeable in this proceedings and it is hereby ORDERED that said debt be not discharged hereby.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that the First National Bank of Broken Arrow shall have and recover judgment from Leslie Steven Kovats upon his Promissory Note in writing dated May 18, 1971, in accordance with the terms and tenor thereof in the amount of $20,838.35, together with interest thereon from November 18, 1971, at the rate of 10% per annum until paid and for a reasonable attorney's fee equal to 15% of the unpaid balance of said note, and for all other costs herein for all of which let execution issue.

DATED this 7th day of March, 1971.

William E. Rutledge, Referee

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF OKLAHOMA

IN THE MATTER OF:

LESLIE STEVEN KOVATS,

Bankrupt.

In Bankruptcy
No. 71-B-871

FINDINGS OF FACT AND CONCLUSIONS OF LAW APPLICABLE TO DETERMINATION OF APPLICATION OF FIRST NATIONAL BANK OF BROKEN ARROW

The following findings of fact and conclusions of law are hereby made and entered relative to the determination of the application filed by the First National Bank of Broken Arrow and the issues raised at hearing thereon.

FINDINGS OF FACT

In October, 1970, the bankrupt delivered to the First National Bank of Broken Arrow a financial statement in connection with a loan of $20,000 made to the bankrupt on October 15, 1970. On such financial statement, the bankrupt knowingly omitted the scheduling of approximately $59,000 in liabilities with the intention of concealing the existence of such liabilites. If the financial statement had been correct, it is likely that the net worth of the bankrupt would have been indicated to be approximately $20,000, and surely no more than $30,000, rather than the $75,000 net worth indicated. Even taking the true net worth of the bankrupt to be the greater amount, the financial statement was materially false in stating the bankrupt's net worth to be $75,000 and in not disclosing the omitted liabilities.

There is a conflict in the evidence as to the time of delivery of the financial statement in October, 1970, and whether the loan of October 15 was made in reliance upon the statement. It is not necessary, however, to resolve this conflict in the determination of the dischargeability of the debt owed to the Bank. Whether the statement was delivered before or after the October 15 loan was made, the bankrupt knew or should have known, that this statement and its import would be of significance in transactions he might have with the Bank subsequent to delivery and that the Bank would be thereby deceived as to his net worth and his liabilities.

The loan of October 15, 1970, matured in six months; it was not paid but was extended for thirty days; and on May 19, 1971, the loan was renewed for six months.

The original loan had been guaranteed by Braden Industries, Inc., the employer of the bankrupt, and the

guaranty extended to the renewal of May 19, 1971. The renewal of the loan of May 19, 1971, was induced by the guaranty as well as by the apparent financial condition of the bankrupt and his net worth as reflected by the statement furnished in October, 1970. It is not possible from the evidence to measure the relative significance of the guaranty and of the statement in inducing the loan, but it will be found that each was significant and, taken together, induced renewal of the loan in May, 1971.

CONCLUSIONS OF LAW

To bar the discharge of a debt under Section 17a.(2) of the Bankruptcy Act upon the basis of a false financial statement, it is not necessary that such statement be the sole inducement for the granting or renewal of credit. It is sufficient if the statement was at least partially relied upon and if it was a contributing cause to the transaction.

It having been found that the renewal of credit in May, 1971, was induced at least in part, by a materially false financial statement issued by the bankrupt with knowledge that the Bank would be deceived as to his net worth and his liabilities, it will be concluded that the debt which was thereby created is not to be discharged in this proceedings and that the Bank is entitled to judgment thereon.

Dated this 3rd day of March, 1972.

/s/ William E. Rutledge

Referee in Bankruptcy

APPENDIX C

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF OKLAHOMA

IN THE MATTER OF:

LESLIE STEVEN KOVATS,

A Bankrupt.

In Bankruptcy

No. 71-B-871
M-534

ORDER

The Court has for consideration the Report and Recommendations of the United States Magistrate reference the Certificate of Review in the above styled matter, and having carefully examined the entire file, being fully advised in the premises, finds:

That the Report and Recommendations of the United States Magistrate should be adopted by this Court.

IT IS, THEREFORE, ORDERED that the Report and Recommendations of the United States Magistrate with reference to the Certificate of Review be adopted by this Court.

ENTERED this 21st day of June, 1972.

/s/ Allen E. Barrow

CHIEF UNITED STATES DISTRICT JUDGE

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF OKLAHOMA

IN THE MATTER OF:
LESLIE STEVEN KOVATS,
A Bankrupt.

In Bankruptcy
No. 71-B-871

REPORT OF UNITED STATES MAGISTRATE

TO THE HONORABLE ALLEN E. BARROW, UNITED STATES DISTRICT JUDGE FOR THE NORTHERN DISTRICT OF OKLAHOMA:

There came on for hearing before the undersigned United States Magistrate in and for the Northern District of Oklahoma on the 12th day of June, 1972, the matter of hearing, by virtue of an Order of Reference made by the Honorable Allen E. Barrow, United States District Judge for the Northern District of Oklahoma, the Petition for Review of the findings, facts and conclusions of law and order entered by the Honorable William E. Rutledge, Referee in Bankruptcy, on the 7th day of March, 1972, pursuant to due notification to counsel of record; the bankrupt appearing by his attorneys, Irvine E. Ungerman and Fred W. Woodson, and the First National Bank of Broken Arrow appearing by its attorney, Roger Scott, and there having been heretofore filed with the Special Master briefs in support of the Petition for Review and in opposition thereto, the undersigned did hear the oral argument of counsel in support of said Petition for Review and in opposition thereto.

Your Magistrate, therefore, recommends to Your Honor that the Petition for Review be sustained and that

the Order of the Referee in Bankruptcy entered herein on the 7th day of March, 1972, should be reversed in its entirety for the following reasons and upon the following grounds, to-wit:

1. That the finding of the Referee in Bankruptcy are clearly erroneous.

2. That the findings of the Referee in Bankruptcy are not supported by the evidence adduced at the hearings on the objections to the discharge of the bankrupt.

3. Your Magistrate finds that the First National Bank of Broken Arrow did not rely upon the statement of financial facts made in writing by the bankrupt, Kovats, at the time that the loan was originally made by the First National Bank of Broken Arrow to Leslie Steven Kovats on October 15, 1970.

4. Your Magistrate further finds that in April, 1971, when the First National Bank of Broken Arrow granted a thirty day extension for the payment of the indebtedness that it did not rely upon any financial statement that it had in its possession and executed by the bankrupt, Leslie Steven Kovats.

5. Your Magistrate further finds that at the time of the execution of the renewal note on June , 1971, that the First National Bank of Broken Arrow did not rely upon any financial statement in its possession and previously given to them by Leslie Steven Kovats as the basis for the renewal of said loan.

6. Your Magistrate further finds that the second financial statement given to First National Bank of Broken Arrow by the bankrupt, Leslie Steven Kovats, was not given to the First National Bank of Broken Arrow

until after the second note was executed and delivered to the bank and the extension of time granted for the payment thereof.

7. Your Magistrate further finds that the loan in controversy was made by the First National Bank of Broken Arrow upon reliance upon a guarantee of payment by Braden Industries, the employer of Kovats, and not upon any financial information furnished by the bankrupt.

8. Your Magistrate further finds that in connection with the thirty-day extension of time granted in April of 1971 that any oral statement made by the bankrupt that there had not been any change in his financial condition was not a statement that was relied upon by the First National Bank of Broken Arrow in extending said loan for a period of thirty days.

9. Your Magistrate further finds that at no time did the First National Bank of Broken Arrow make any investigation whatsoever as to the financial condition of Leslie Steven Kovats, the bankrupt herein, but relied upon the guaranty that it had from Braden Industries which guaranteed the payment of a loan that had been arranged for by Braden Industries with First National Bank of Broken Arrow and had been made to the bankrupt as the result of said arrangement.

IT IS THEREFORE RECOMMENDED TO THE HONORABLE ALLEN E. BARROW, UNITED STATES DISTRICT JUDGE FOR THE NORTHERN DISTRICT OF OKLAHOMA, by the undersigned United States Magistrate for the Northern District of Oklahoma, to whom this matter has been referred for hearing, that the Petition for Review of the Referee's findings, order and judgment entered herein on the 7th day of March, 1972,

should be sustained, and that the judgment entered herein by the Referee denying a discharge in bankruptcy to Leslie Steven Kovats of the indebtedness listed as due and owing to the First National Bank of Broken Arrow should be reversed in its entirety, and a discharge in bankruptcy of said claim of First National Bank of Broken Arrow be granted to Leslie Steven Kovats, the bankrupt herein, and that the judgment rendered in favor of the First National Bank of Broken Arrow against Leslie Steven Kovats by the Referee herein on the 7th day of March, 1972, should be vacated, set aside and held for naught.

Respectfully submitted,

United States Magistrate

/s/ ~~Marion R.~~ MORRIS L. Bradford

APPENDIX D

Title 11, United States Code, Sec. 35(a)(2):

> "A discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as...(2) are liabilities for obtaining money or property by false pretenses or false representations, or for obtaining money or property on credit or obtaining an extension or renewal of credit in reliance upon a materially false statement in writing respecting his financial condition made or published or caused to be made or published in any manner whatsoever with intent to deceive, or for willful and malicious conversion of the property of another;..."

Title 11, United States Code, Sec. 32(c):

> "The court shall grant the discharge unless satisfied that the bankrupt has (1) committed an offense punishable by imprisonment as provided under section 152 of Title 18; or (2) destroyed, mutilated, falsified, concealed, or failed to keep or preserve books of account or records, from which his financial condition and business transactions might be ascertained, unless the court deems such acts or failure to have been justified under all the circumstances of the case; or (3) while engaged in business as a sole proprietor, partnership, or as an executive of a corporation, obtained for such business money or property on credit or as an extension or renewal of credit by making or publishing or causing to be published in any manner whatsoever a materially false statement in writing respecting his financial condition or the financial condition of such partnership or corporation; or (4) at any time subsequent to the first day of the twelve months immediately preceding the filing of the

petition in bankruptcy, transferred, removed, destroyed, or concealed, or permitted to be removed, destroyed, or concealed, any of his property with intent to hinder, delay, or defraud his creditors; or (5) in a proceeding under this title commenced within six years prior to the date of the filing of the petition in bankruptcy has been granted a discharge, or had a composition or an arrangement by way of composition or a wage earner's plan by way of composition confirmed under this title; or (6) in the course of a proceeding under this title refused to obey any lawful order of, or to answer any material question approved by, the court; or (7) has failed to explain satisfactorily any losses of assets or deficiency of assets to meet his liabilities; or (8) has failed to pay the filing fees required to be paid by this title in full: *Provided*, That if, upon the hearing of an objection to a discharge, the objector shall show to the satisfaction of the court that there are reasonable grounds for believing that the bankrupt has committed any of the acts which, under this subdivision, would prevent his discharge in bankruptcy, then the burden of proving that he has not committed any of such acts shall be upon the bankrupt."

CERTIFICATE OF SERVICE

The undersigned attorney of record for the Petitioner here, Leslie Steven Kovats, hereby certifies that on the _____ day of September, 1973, in compliance with Rule 33(1) of the Rules of the Supreme Court of the United States, three copies of the foregoing Petition for Writ of Certiorari were deposited in the United States Post Office at Tulsa, Oklahoma, with first class postage prepaid, addressed to the following counsel of record at his Post Office address as shown:

Roger R. Scott,
Attorney for First National Bank of
Broken Arrow,
Fourth National Bank Building
Tulsa, Oklahoma 74119

_____
Irvine E. Ungerman

SUPREME COURT, U. S.

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1973

No. 73-485

IN THE MATTER OF
LESLIE STEVEN KOVATS, Bankrupt,
Petitioner,

vs.

FIRST NATIONAL BANK OF BROKEN ARROW,
Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS TENTH CIRCUIT

ROGER R. SCOTT
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Attorneys for Respondent

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IN THE
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No. 73-485

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RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS TENTH CIRCUIT

TO THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

First National Bank of Broken Arrow, Respondent herein, opposes the Petition for Writ of Certiorari to the United States Court of Appeals, Tenth Circuit, filed by Leslie Steven Kovats. The reasons for this opposition are hereinafter set forth. Respondent contends the opinion of the Court of Appeals, Tenth Circuit, contained in Appendix A to the Petition is a correct decision which raises no considerations described in Rule 19 of this Court, which raises no issue of law of public importance and in fact raises no issue properly reviewable by Writ of Certiorari. The con-

siderations described by Petitioner involve only questions of fact and sufficiency thereof and no issue or question of law is involved. For these reasons and those stated below, the Petition for Writ of Certiorari should be denied.

STATEMENT OF THE CASE

The complete facts are these:

It is undisputed that Leslie Steven Kovats, Petitioner herein, executed a promissory note in writing to the Bank bearing a date of October 15, 1970 in the amount of $20,000.00, for a term of six (6) months. In connection with the execution of the note and the loan from the Bank, the Petitioner also tendered the Bank a financial statement in writing, signed by the Bankrupt, which the evidence indisputably revealed overstated the Petitioner's net worth by approximately $59,000.00 with the result that the Petitioner's true net worth was less than the amount of money which he was seeking to borrow from the Bank. The Petitioner admitted he omitted those liabilities on purpose and did not intend to disclose their existence. There was a conflict in the evidence as to whether that financial statement was in fact given on October 15, 1970 or whether it was delivered to the Bank a few days thereafter.

Subsequently, the loan was renewed for a 30 day period and thereafter was renewed for an additional six (6) months by the Bank as evidenced by a new note signed by the Petitioner. At the time the loan was renewed, an inquiry was made of the Petitioner concerning his financial condition and he assured the Bank that the financial statement previously given still reflected his true financial condition. In extending or renewing the loan to the Petitioner on May 19, 1971, the Bank relied solely upon that financial statement in determining the Petitioner's financial condi-

tion, and the testimony was undisputed that the Bank had no other information concerning the Petitioner's alleged financial position.

In connection with the original loan and the renewals thereof, the Bank also obtained, as additional collateral, the guaranty of Braden Industries, Inc. of Broken Arrow, Oklahoma, the employer of Petitioner. (Kovats was financial Vice-President of Braden and had extensive experience in corporate financial affairs.) However, the testimony revealed that at the time the loan was renewed in May, 1971, the Bank was aware, as was the Petitioner, that his position with Braden was precarious. The President of the Bank testified that he was relying solely upon the Petitioner to repay the loan although he admitted that he would not have made the loan without the Braden guaranty as additional collateral. He also testified that he would not have made the loan, even with the Braden guaranty, had he known the true financial condition of the Petitioner.

At the conclusion of the testimony, the Referee made certain findings of fact and conclusions of law including a finding that the Petitioner uttered a false financial statement understating his liabilities in the amount of approximately $59,000.00 with the intention of concealing the existence of such liabilities. The Referee declined to resolve the conflict as to whether the financial statement was originally tendered the Bank on October 15, 1970, the date the loan was originally funded, or whether it was delivered later as claimed by the Petitioner. He found it unnecessary to resolve that conflict since the record was clear that the Petitioner knew or should have known that the financial statement and its import of significance in transactions he might

have with the Bank subsequent to the delivery thereof and that the Bank would be thereby deceived as to his net worth and liabilities. The Referee further found that the renewal of the loan on May 19, 1971 was induced by the guaranty of Braden Industries as well as the apparent financial condition of the Petitioner and his net worth as reflected on the financial statement furnished in October, 1970. The Referee found that it was not possible to measure the relative significance of the Braden guaranty and the financial statement in inducing the loan, but the Referee found that each was significant and taken together induced the renewal of the loan in May, 1971. He further found it was not necessary that the financial statement uttered by the Petitioner be the sole inducement for the granting of renewal of the credit. Thereupon, the Referee concluded the debt owed by the Petitioner to the Bank was non-dischargeable under Section 17 a (2) of the Bankruptcy Act and entered judgment thereon.

Kovats then petitioned the United States District Court under a Petition for Review requesting that the Referee's findings and conclusions be reviewed by the District Court assigning among certain specified grounds of error that the Referee's findings were "clearly erroneous" and not sustained by the evidence. The District Court found that the Referee's findings and conclusions were "clearly erroneous" and held the debt to be discharged. However, the District Court did not hear any additional evidence or testimony but made its determination solely from the record and upon arguments of counsel.

In reversing the District Court, the United States Court of Appeals, Tenth Circuit, found the District Court erred in at least two ways:

1. The District Court re-tried the case de novo and did not confine its inquiry as an appellate tribunal required by General Order 47.
2. The evidence did not require the Referee to resolve the conflict as to when the financial statement was actually delivered to the Bank. The Bank had only one financial statement of the Petitioner when the Bank extended or renewed the loan and under Section 17(a) the debt was nondischargeable.

ARGUMENT

REASONS WHY THE WRIT SHOULD NOT ISSUE

As this Court has numerously stated, certiorari should not be granted except in cases involving principles the settlement of which is of importance to the public, as distinguished from that of the parties and in cases where there is a real and embarrassing conflict of opinion and authority between the Courts of Appeal. E.g., *Layne & Bowler Corporation* v. *Western Well Works*, 261 U.S. 387 (1923).

THE PETITION FAILS TO STATE CONSIDERATIONS SET FORTH IN RULE 19

Rule 19 of this Court, while not fully measuring the Court's discretion, sets forth the character of the reasons which will be considered in a review on Writ of Certiorari. Additionally, the Rule re-emphasizes that certiorari is not a matter of right but of sound judicial discretion and will be granted only where there are special and important reasons therefor. It is submitted that Kovat's Petition does not set forth any of the enumerated reasons and most certainly does not raise any principle of importance to the public nor any special and important reason.

This is not a case involving a state court decision of a federal question and hence, this ground is unavailable to seek certiorari. Nor is this a situation where a Court of Appeals has decided an important state question in conflict with applicable state law, nor a case involving an important question of federal law which has not been, but should be settled by this Court. Also, this is not a situation where a lower Court has decided a federal question in conflict with the decisions of this Court or has so far departed from the accepted and usual course of judicial proceedings. In short, nothing has been raised by Petitioner sufficient to invoke this Court's supervisory powers.

There is no conflict between decisions of the Courts of Appeal. In fact, the instant case is in accord with for the prior decisions of the Courts of Appeals, Tenth Circuit, Ninth Circuit and the Second Circuit. See *Clancy* v. *First National Bank of Colorado*, 408 F.2d 899 (10th Cir. 1969) cert. den. 396 U.S. 958; *Wylie* v. *Ward*, 292 F.2d 500 (9th Cir. 1961); *Lloyd* v. *Industrial Bank*, 241 F.2d 924 (2nd Cir. 1957).

The Tenth Circuit totally rejected the argument made by Petitioner that it was necessary for the Referee to determine when the financial statement was given with respect to the original loan. The Court accurately noted that such argument flies in the face of the undisputed facts and the law. Section 17 (a) of the Bankruptcy Act, the Court noted, creates a bar to dischargeability if there is:

> "...'an extension or *renewal of credit* in reliance upon a materially false statement in writing respecting his financial condition' [Emphasis Added]" (See Appendix A p. A5, Petition for Writ of Certiorari.)

The Court held total reliance upon the statement is not required; the statement need only be a substantial factor in bringing about the extension of credit. The record in this case clearly revealed that the false financial statement given by Kovats was the only written financial information in the Bank's possession when the loan was renewed and Kovats knew the Bank was going to rely upon the statement when the loan was to be renewed. This, the Tenth Circuit concluded, satisfies the requirements of Section 17 (a) of the Bankruptcy Act.

It is an inescapable conclusion that one who utters an intentionally false financial statement must be deemed to have uttered it with the intent to deceive. The Court of Appeals agreed with the Referee that Kovats knew or should have known that the Bank was going to rely upon the statement in any renewals of the loan. The transcript of the testimony supports such a finding. One must be presumed to have intended the necessary consequences of his own voluntary acts. Where a false statement in its nature calculated to defraud is made with knowledge of its falsity, intent will be inferred. See *Beneficial Finance Company of Charleston* v. *Collins*, 149 S.E.2d 221 (W. Va. 1966).

It is ridiculous to say that Kovats lacked an intent to deceive the Bank. If, as he contended, the loan had been made prior to tendering the financial statement why would he bother to make a false statement? He already had the money. It is obvious however, that if a true statement had been rendered the loan would not have been renewed at the end of the six month term. This Kovats knew or should have known. His own testimony supported a finding that he expected to renew the loan upon expiration of the original six month term. Intent is a question of fact, not a question of law. The Tenth Circuit found:

> "After reviewing the record on appeal, we find there is *substantial evidence* to support the Referee's findings of an intent by Kovats to deceive, and reliance by the Bank on the false financial statement when renewing the loan in question". [Emphasis supplied].

This substantial evidence alleviated the need to resolve the conflict as contended by Petitioner.

The fourth question presented for review is a smokescreen. Assuming arguendo that the Court of Appeals (and the Referee) adopted a standard of proof contrary to one adopted by the Supreme Court of Oklahoma, nevertheless such is not a basis for certiorari, let alone for an appeal. A bankruptcy court or other federal court does not necessarily apply the law the state where it sets but applies the Bankruptcy Act as interpreted by authoritative federal decisions in determining questions of dischargeability. See CJS Federal Courts 169 (b). *In re Chicago Rapid Transit Co.*, 129 F.2d 1 (7th Cir. 1942).

ADDITIONAL SUPPORT FOR TENTH CIRCUIT DECISION

In addition to reversing the District Court on the grounds stated above, the Tenth Circuit reversed upon the additional ground that the District Court failed to function in an appellate posture, as required by General Order in Bankruptcy 47. The Court correctly held that in applying this General Order the District Court's function is not to decide factual issues de novo. See *Zenith Radio Corp.* v. *Hazeltine Research, Inc.* 395 U.S. 100 (1969). Rather the Court noted, the District Court must review the findings and conclusions giving deference to the trier of fact who is in a superior position to weigh the

evidence. The Court then stated such rule is especially true in the instant case where the District Court did not take further testimony but only heard arguments of counsel. Cf. *Washington* v. *Houston Lumber Co.*, 310 F.2d 881 (10th Cir. 1962); *Dailey* v. *City of Lawton, Oklahoma*, 425 F.2d 1037 (10th Cir. 1970).

THE TENTH CIRCUIT OPINION RAISES NO ISSUES OF PUBLIC IMPORTANCE

The opinion of the Court of Appeals is well founded upon prior case law both in that Circuit and other Circuits. The case was apparently not regarded by that Court as establishing new precedent since that Court ordered the opinion not be published. The case involves a clear application of facts to established principles of law. No new precedent was established; rather the Court of Appeals reversed the District Court on two distinct grounds, both of which involved questions of fact. Rule 19 addresses itself to questions of law rather than questions of fact. Rather than urge to this Court any of the considerations recognized as a grounds for a Writ of Certiorari Petitioner has attempted again to appeal that the lower Court erred.

In summary, the Petitioner has failed to raise any issue or principle of importance to the public. He is seeking only to overturn a personal money judgment which has correctly been entered against him. No special or important reasons have been urged by Petitioner for

the review he is requesting. The Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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2910 Fourth National Bank Building
Tulsa, Oklahoma 74119

Attorney for Respondent

CERTIFICATE OF SERVICE

The undersigned attorney of record for the Respondent here, First National Bank of Broken Arrow, hereby certifies that on the 12th day of October, 1973, in compliance with Rule 33(1) of the Rules of the Supreme Court of the United States, three copies of the foregoing Respondent's Brief in Opposition to Petition for Writ of Certiorari were deposited in the United States Post Office at Tulsa, Oklahoma, with first class postage prepaid, addressed to the following counsel of record at his Post Office address as shown:

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Roger R. Scott